

In the Supreme Court of the United States E D

OCTOBER TERM, 1990

COY R. GROGAN, ET AL., PETITIONERS

v.

FRANK J. GARNER, JR.

Supreme Court, U.S.
JUL 3 1990
JOSEPH F. SPANIOL, JR.
CLERKON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUITBRIEF FOR THE UNITED STATES,
THE SECURITIES AND EXCHANGE COMMISSION,
AND THE
FEDERAL DEPOSIT INSURANCE CORPORATION
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QUESTION PRESENTED

Whether a claim that a debt arises from "false pretenses, a false representation, or actual fraud," and so is excepted from discharge under Section 523(a) of the Bankruptcy Code, must be proved by a preponderance of the evidence or by clear and convincing evidence.

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No. 89-1149

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v.

FRANK J. GARNER, JR.

**ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT**

**BRIEF FOR THE UNITED STATES,
THE SECURITIES AND EXCHANGE COMMISSION,
AND THE
FEDERAL DEPOSIT INSURANCE CORPORATION
AS AMICI CURIAE SUPPORTING PETITIONERS**

**INTEREST OF THE UNITED STATES, THE
SECURITIES AND EXCHANGE COMMISSION, AND
THE FEDERAL DEPOSIT INSURANCE CORPORATION**

The Court's resolution of the question presented in this case will affect the civil enforcement of federal antifraud statutes by the United States, the Securities and Exchange Commission (SEC), and the Federal Deposit Insurance Corporation (FDIC), as well as other federal agencies. The United States obtains money judgments under the False Claims Act, 31 U.S.C. 3729-3731, against persons who defraud the federal government. The False Claims Act expressly provides that the government need prove fraud only by a preponderance of the evidence. 31 U.S.C. 3731(c).

(1)

The SEC obtains judgments, under a preponderance of the evidence standard, for violations of the antifraud provisions of the federal securities laws. See *Herman & MacLean v. Huddleston*, 459 U.S. 375, 389 (1983). The SEC's interest in this case arises not only because of the agency's role in obtaining monetary relief in its own enforcement actions, but also because private actions under the federal securities laws are a necessary supplement to the SEC's enforcement actions, see *Basic Inc. v. Levinson*, 485 U.S. 224, 230-231 (1988), and because the SEC acts as advisor to the courts in bankruptcy reorganization cases pursuant to Section 1109(a) of the Bankruptcy Code, 11 U.S.C. 1109(a).

The FDIC and the Resolution Trust Corporation (RTC) obtain money judgments against persons who defraud federally insured financial institutions.¹ The FDIC proceeds under a variety of antifraud laws that require proof only by a preponderance of the evidence, including the enforcement provisions of the Federal Deposit Insurance Act (FDIA), 12 U.S.C. 1818(i), the director and officer liability provisions of the FDIA, 12 U.S.C. 1821 (k)-(l), the civil provisions of the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. 1964, and the antifraud provisions of the securities laws and the Commodity Exchange Act (CEA), 7 U.S.C. 1 *et seq.* Moreover, Congress expressly provided in 12 U.S.C. 1833a(e) that the preponderance standard applies to actions brought by the Attorney General to recover civil penalties for certain fraudulent conduct involving financial institutions.²

¹ Congress created the RTC "to contain, manage, and resolve failed savings associations." Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, § 101(7), 103 Stat. 183.

² Other federal agencies also obtain civil fraud remedies under a preponderance of the evidence standard. For example, a preponderance standard applies to Medicare and Medicaid fraud

If the Court were to hold that proof of fraud under Section 523(a) must be by clear and convincing evidence, fraud judgments obtained after a full trial on the merits under a preponderance of the evidence standard would not be recognized in bankruptcy courts. Victims of fraud would therefore be required to prove fraud a second time, by clear and convincing evidence, in the bankruptcy proceedings. Such proceedings would be costly to the victims and burdensome to the bankruptcy courts. The United States, the SEC, the FDIC, and other federal agencies have a strong interest in opposing a rule that imposes such an unwarranted burden on victims of fraud, and in preventing the bankruptcy courts from becoming a haven for wrongdoers.

STATEMENT

1. Petitioners were employees and minority shareholders of STI-Missouri, a corporation that repaired and refurbished railroad rolling stock. Respondent was the president and majority shareholder of the corporation. Petitioners sued respondent in the United States District Court for the Western District of Missouri, alleging that respondent had defrauded them in connection with the sale of securities of STI-Missouri and another corporation. Petitioners sought damages for violations of the antifraud provisions of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), as well as for

claims. See 42 U.S.C. 1320a-7a; 42 C.F.R. 1003.114(a). In addition, where the Internal Revenue Service establishes that any part of a tax underpayment is attributable to fraud, the entire underpayment is subject to fraud penalties unless the taxpayer establishes, by a preponderance of the evidence, that the underpayment is not attributable to fraud. See Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, § 7721(a), 103 Stat. 2395 (to be codified at 26 U.S.C. 6663(b)). The Commodity Futures Trading Commission's findings of violations of the anti-fraud provisions of the CEA also are reviewed under a preponderance standard. See *Lawrence v. CFTC*, 759 F.2d 767, 773 (9th Cir. 1985).

common law fraud and breach of fiduciary duty. The case was tried before a jury. The district court did not specifically instruct the jury as to the applicable standard of proof. Instead, it instructed the jury generally that “[i]f the evidence in the case does not cause you to believe a particular proposition submitted, then you cannot return a verdict requiring belief of the proposition.” Pet. App. 24a. The jury returned a verdict for petitioners, awarding damages on all counts and punitive damages on the common law fraud count. The Court of Appeals for the Eighth Circuit reduced the amount of damages, but otherwise affirmed the judgment for petitioners. *Grogan v. Garner*, 806 F.2d 829 (1986). See Pet. App. 3a-5a, 16a-17a, 30a-31a.

2. In October 1985, while respondent's appeal of the fraud judgment was pending in the court of appeals, respondent filed a petition in the United States Bankruptcy Court for the Western District of Missouri for relief under Chapter 11 of the Bankruptcy Code, 11 U.S.C. 1101 *et seq.* The petition listed the fraud judgment as a dischargeable debt. In May 1986, petitioners filed a complaint in the bankruptcy court for a determination that their judgment debt should be excepted from discharge pursuant to Section 523 of the Bankruptcy Code, 11 U.S.C. 523.³ At the trial on their complaint, petitioners

³ Section 523 provides, in part:

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt—

* * * *

(2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

(B) use of a statement in writing—

submitted copies of relevant pleadings and documents from the prior fraud action, including the complaint, the jury instructions, the district court's judgment, and the court of appeals' decision. The bankruptcy court determined that each of the elements necessary to establish “actual fraud” under Section 523 had been proved in the prior action. Applying principles of collateral estoppel, the court held that the judgment debt was not dischargeable under Section 523(a)(2)(A). The bankruptcy court rejected respondent's contention that collateral estoppel did not apply because the jury in the prior fraud action had not been instructed that fraud must be proved by clear and convincing evidence. The bankruptcy court concluded that there was no real distinction between the preponderance of the evidence standard and the clear and convincing evidence standard. Pet. App. 3a-4a, 18a-20a, 31a, 40a. The district court agreed with the reasoning of the bankruptcy court and affirmed its judgment. Pet. App. 16a-29a.

3. The Court of Appeals for the Eighth Circuit reversed. The court stated that the standard of proof necessary to establish an exception from discharge under Section 523(a) is “far from clear,” recognizing that those courts of appeals requiring proof by clear and convincing evidence often have done so without a satisfactory ex-

- (i) that is materially false;
- (ii) respecting the debtor's or an insider's financial condition;
- (iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and
- (iv) that the debtor caused to be made or published with intent to deceive.

In addition, Section 523(a)(4) of the Bankruptcy Code, 11 U.S.C. 523(a)(4), excepts from discharge in bankruptcy any debt “for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.”

planation. Pet. App. 9a-12a. Moreover, the court recognized, neither the language of Section 523 nor its legislative history addresses the issue. Pet. App. 13a. The court nevertheless held that the statutory exception to discharge for fraud must be proved by clear and convincing evidence rather than by a preponderance of the evidence. The court surmised that Congress was aware "that the prevailing view at the time of adoption was that fraud, for both section 523 and state common law purposes, had to be proved by clear and convincing evidence." *Ibid.* The court also stated that a preponderance of the evidence standard of proof would "effectively read[] the 'fresh start' policy out of * * * the Code." *Ibid.* Because the preponderance standard is a lower standard than the clear and convincing evidence standard, the court of appeals held that the bankruptcy court had erred in giving collateral estoppel effect to the prior fraud judgment. Pet. App. 9a-10a, 12a, 14a.

SUMMARY OF ARGUMENT

1. a. Neither the Bankruptcy Code nor its legislative history expressly prescribes the standard of proof applicable to a claim that a debt arises from the debtor's fraudulent conduct and therefore is excepted from discharge under Section 523(a) of the Code. In the absence of any contrary expression, the most natural inference is that Congress intended such claims to be subject to the preponderance of the evidence standard generally applicable in civil proceedings. The debtor's interest in obtaining a discharge of debts arising from fraudulent conduct is not a constitutional or fundamental individual right that warrants application of a heightened standard of proof. In any event, Congress has determined that the "fresh start" provided by a discharge is available only to honest debtors, and has recognized, in Section 523(a), a countervailing and equally important interest of the victims of fraud in preserving their right to recover from dishonest debtors. Thus, there is no basis for concluding

that a defrauding debtor's interest in a complete discharge takes precedence over the innocent victim's interest and, consequently, no basis for favoring the debtor by creating an exception to the general rule of proof and applying a clear and convincing evidence standard. The court below therefore erred when it reasoned that the preponderance of the evidence standard in this context would "read[] the 'fresh start' policy out of * * * the Code." Pet. App. 13a. Congress *wrote* that policy out of the Code with respect to debts arising from fraud when it enacted Section 523.

b. To the extent that the Bankruptcy Code and its legislative history shed light on the question, they support application of the typical preponderance standard. The legislative history of Section 727 of the Bankruptcy Code states that the bankruptcy court, in a Chapter 7 proceeding, may deny the debtor a discharge as to *all* debts if it is shown, by a preponderance of the evidence, that the debtor has engaged in certain fraudulent conduct in connection with the bankruptcy proceeding. There is no reason to suppose that Congress would apply a higher standard of proof to the less important question whether a particular debt should be excepted from discharge because of fraud. In addition, application of the clear and convincing standard in this context would depart from the standard of proof in important federal antifraud statutes that require proof only by a preponderance of the evidence. The result would be that some persons determined to be guilty of fraud under important congressional enactments would escape liability by declaring bankruptcy, either because plaintiffs would elect not to devote the resources to trying the case a second time, or because plaintiffs, who would often be forced to present stale evidence, could not reprove fraud by clear and convincing evidence. There is no evidence that Congress intended such a result. On the contrary,

the basic intent of Section 523(a) is that debtors *not* escape liability for fraud. This Court should not embrace such an outcome, when the more natural application of the typical preponderance rule avoids this troubling anomaly.

2. The court below based its decision on a “presum[ption]” that Congress was aware when it enacted Section 523 that the “prevailing view” was that fraud had to be proved by clear and convincing evidence. Pet. App. 13a. In fact, there was no consistent pre-Code practice of requiring clear and convincing proof either to establish fraud or to prove that a debt was incurred by fraud. State courts were then and are now divided over the appropriate standard of proof in civil actions for fraud. At the time Section 523 was enacted, some courts required that fraud exceptions to discharge be proved by clear and convincing evidence, while others applied the preponderance standard. Thus, even if Congress should be “presumed” to be aware of existing law in the absence of any evidence that the pertinent body of law was called to its attention, Congress cannot be assumed to have understood that fraud had to be proved by clear and convincing evidence. Moreover, the original reasons for applying a higher standard of proof in certain equitable actions for fraud have little or no application to modern fraud actions for damages.

ARGUMENT

I. THE PREPONDERANCE OF THE EVIDENCE STANDARD APPLIES IN ACTIONS UNDER SECTION 523(a) OF THE BANKRUPTCY CODE TO EXCEPT FROM DISCHARGE DEBTS INCURRED BY FRAUD

Section 523(a)(2) of the Bankruptcy Code, 11 U.S.C. 523(a)(2), excepts from discharge in bankruptcy any debt of an individual debtor that arises from that debtor's fraudulent conduct.⁴ The court of appeals held that a creditor seeking to except a claim from discharge under Section 523(a)(2) must prove fraud by clear and convincing evidence. Under the court of appeals' decision, principles of collateral estoppel would not apply where, as here, a prior fraud judgment was obtained under a preponderance of the evidence standard. This is an unwarranted result. A plaintiff who has proved fraud in a nonbankruptcy court need not, and should not, be required to retry the case in the bankruptcy court to preserve the prior judgment from discharge.⁵

⁴ See note 3, *supra*.

⁵ We agree with the courts below that principles of collateral estoppel apply in bankruptcy proceedings. See Pet. App. 6a-7a, 35a-36a. Although the Court formally reserved this question in *Brown v. Felsen*, 442 U.S. 127 n.10 (1979), it subsequently stated that “[i]n many cases * * * principles of issue preclusion would obviate the need for a bankruptcy court to reexamine factual questions.” *Kelly v. Robinson*, 479 U.S. 36, 48 n.8 (1986). Collateral estoppel, unlike the doctrine of res judicata at issue in *Brown v. Felsen*, *supra*, applies only to those factual issues actually and necessarily determined in prior litigation between the parties. See *Montana v. United States*, 440 U.S. 147, 153 (1979); *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326 n.5 (1979). Consequently, there is no danger that bankruptcy issues will be determined in cases where the parties lack an adequate incentive to litigate them. Where, as here, factual issues are actually litigated in nonbankruptcy courts, application of collateral estoppel principles is appropriate and fully consistent with the prior decisions of this Court. See generally *Heiser v. Woodruff*, 327 U.S. 726 (1946);

A. In a Proceeding to Except from Discharge a Debt Incurred by Fraud, the Balance of Interests of the Parties Requires Application of the Preponderance of the Evidence Standard

1. Section 523 does not prescribe the standard of proof applicable to claims that a debt is excepted from discharge because of the debtor's fraudulent conduct. The legislative history of Section 523 and its predecessor, Section 17 of the Bankruptcy Act 11 U.S.C. 35 (1976), also are silent on this issue.⁶ Where Congress has not specified a standard of proof, and the Constitution does not require a particular standard, the courts will fill the gap. See *Herman & MacLean v. Huddleston*, 459 U.S. 375, 389 (1983); *Steadman v. SEC*, 450 U.S. 91, 95 (1981).⁷

Fischer v. Pauline Oil & Gas Co., 309 U.S. 294, 302-303 (1940); *Davis v. Friedlander*, 104 U.S. 570 (1881). Virtually every court of appeals to consider the question has held that collateral estoppel is applicable in discharge exception proceedings. See *In re Braen*, 900 F.2d 621 (3d Cir. 1990); *Combs v. Richardson*, 838 F.2d 112, 114 (4th Cir. 1988); *Klingman v. Levinson*, 831 F.2d 1292 (7th Cir. 1987); *In re Shuler*, 722 F.2d 1253, 1256 (5th Cir.), cert. denied, 469 U.S. 817 (1984); *Lovell v. Mixon*, 719 F.2d 1373, 1376 (8th Cir. 1983); *Spilman v. Harley*, 656 F.2d 224, 226 n.2 (6th Cir. 1981). See also *In re Lombard*, 739 F.2d 499, 503 (10th Cir. 1984) (collateral estoppel applies at least where the bankruptcy court does not have exclusive jurisdiction). But cf. *In re Houtman*, 568 F.2d 651 (9th Cir. 1978) (judgment of a nonbankruptcy court establishes only *prima facie* case of non-dischargeability).

We also agree with the court of appeals that collateral estoppel applies in this case only if Section 523(a) requires proof of fraud by a preponderance of the evidence. See *Price Waterhouse v. Hopkins*, 109 S. Ct. 1775 (1989).

⁶ See S. Rep. No. 989, 95th Cong., 2d Sess. 77-80 (1978); H.R. Rep. No. 595, 95th Cong., 1st Sess. 129-132, 363-365 (1977); S. Rep. No. 1173, 91st Cong., 2d Sess. (1970); H.R. Rep. No. 1502, 91st Cong., 2d Sess. (1970); H.R. Rep. No. 1409, 75th Cong., 1st Sess. (1937); S. Rep. No. 1916, 75th Cong., 3d Sess. (1938).

⁷ The determination whether a debt is excepted from discharge under Section 523(a) is a matter of federal bankruptcy law. See

The function of a standard of proof is to "allocate the risk of error between the litigants and to indicate the relative importance attached to the ultimate decision." *Addington v. Texas*, 441 U.S. 418, 423 (1979). The standard of proof performs this function by "instruct[ing] the factfinder concerning the degree of confidence our society thinks he should have in the correctness of factual conclusions." *Ibid.* (quoting *In re Winship*, 397 U.S. 358, 370 (1970) (Harlan, J., concurring)). The preponderance standard is the only standard of proof that results in a roughly equal allocation of the risk of error between the parties; "[a]ny other standard expresses a preference for one side's interests." *Huddleston*, 459 U.S. at 390; *Addington v. Texas*, 441 U.S. at 423.⁸ Consequently, the Court has recognized that the "preponderance-of-the-evidence standard [is] generally applicable in civil actions," unless "particularly important individual interests or rights are at stake." *Huddleston*, 459 U.S. at 389-390. See also *Santosky v. Kramer*, 455 U.S. 745, 756 (1982); *Addington v. Texas*, 441 U.S. at 423.⁹ Where no constitutional or other very important

Brown v. Felsen, 442 U.S. at 136. Accordingly, the standard of proof in a Section 523(a) proceeding is also a matter of federal law.

⁸ A heightened standard of proof not only increases the probability that an error will favor the debtor, but also increases the overall probability of an erroneous decision. See Winter, *The Jury and the Risk of Nonpersuasion*, 5 Law & Soc. Rev. 335, 337 (1970); Ball, *The Moment of Truth: Probability Theory and Standards of Proof*, 14 Vand. L. Rev. 807, 816-817 (1961).

⁹ The Court has required proof by clear and convincing evidence only where constitutional or other highly important individual interests are at stake. See, e.g., *Santosky v. Kramer*, *supra* (proceeding to terminate parental rights); *Addington v. Texas*, *supra* (involuntary civil commitment proceedings); *Boddie v. Connecticut*, 401 U.S. 371 (1971) (right to sue for divorce); *Woodby v. INS*, 385 U.S. 276 (1966) (determination of alien's deportability); *New York Times v. Sullivan*, 376 U.S. 254 (1964) (First Amendment rights); *Chaunt v. United States*, 364 U.S. 350 (1960) (proceeding to revoke United States citizenship); *Schneiderman v. United*

individual right is implicated, the Court has applied the preponderance standard, even where severe civil sanctions may be imposed. See, e.g., *Huddleston*, 459 U.S. at 389-390; *Steadman v. SEC*, *supra* (proceeding to permanently bar individual, on grounds of fraud, from securities industry); *United States v. Regan*, 232 U.S. 37, 48-49 (1914) (civil suit that may expose defendant to criminal prosecution). In this case, as in *Huddleston*, “the balance of interests *** warrants use of the preponderance standard.” 459 U.S. at 390.

2. A discharge in bankruptcy affords the debtor “a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.” *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934). But Congress has made this fresh start available only to “the honest debtor.” *Ibid.* In enacting Section 523(a), Congress determined that the fresh start policy should not override an innocent victim’s interest in obtaining redress for fraud. As the Court observed in the context of another exception to discharge, the fresh start policy “cannot override the specific policy judgments made by Congress in enacting the [exceptions to discharge].” *United States v. Sotelo*, 436 U.S. 268, 279 (1978); see also 1 D. Cowans, *Cowans Bankruptcy Law and Practice* § 6.2, at 691-692 (1989) (the fresh start policy “is not so important *** as to negate other important policies which the law feels a responsibility to foster and abet”).

This Court has held that the debtor’s interest in obtaining a discharge is not a constitutional right or a fundamental interest. In *United States v. Kras*, 409 U.S. 434, 446 (1973), the Court held that “[t]here is no constitutional right to obtain a discharge of one’s debts in

States, 320 U.S. 118, 125, 159 (1943) (denaturalization proceedings). See also *Cruzan v. Director, Missouri Dep’t of Health*, No. 88-1503 (June 25, 1990) slip op. 17-19 (State may require clear and convincing proof of patient’s choice to discontinue life-sustaining treatment).

bankruptcy.” Because the Court saw “no fundamental interest that is gained or lost depending on the availability of a discharge in bankruptcy,” *id.* at 445, it held that a debtor who fails to pay bankruptcy court fees may be denied a discharge of *all* debts. The more limited question whether a particular debt is subject to discharge can hardly rise above the level of importance of the complete denial of a discharge in bankruptcy at issue in *Kras*.

On the other hand, the innocent victim’s interest in obtaining compensation for fraud is at least as important as the defrauding debtor’s interest in obtaining a fresh start. The policy against discharging debts incurred by fraud is deeply embedded in the bankruptcy law, and has been recognized in every bankruptcy statute since the Act of March 2, 1867.¹⁰ In this case, moreover, petitioners are “among the very individuals Congress sought to protect in the securities laws.” *Huddleston*, 459 U.S. at 390.

In short, Section 523(a)(2) represents a congressional judgment that certain wrongful conduct by a debtor should *not* be forgiven in bankruptcy. In deciding whether such wrongful conduct has been shown, there is no indication that Congress intended to tip the scales in favor of the debtor and against the victim of fraud. Judicial implication of a standard of proof favoring the

¹⁰ See Act of Mar. 2, 1867, ch. 176, § 33, 14 Stat. 517; Act of July 1, 1898, ch. 541, § 17, 30 Stat. 550; Act of June 22, 1938, ch. 575, § 17a, 52 Stat. 840. In the 1898 statute, Congress provided that “judgments” sounding in fraud were excepted from discharge. In 1903, Congress substituted the term “liabilities” for “judgments.” Act of Feb. 5, 1903, ch. 487, § 5, 32 Stat. 798. As the Court has noted, the 1903 amendment was intended to broaden the category of claims excepted from discharge. *Brown v. Felsen*, 442 U.S. at 138 (quoting H.R. Rep. No. 1698, 57th Cong., 1st Sess. 3, 6 (1902)). In this case, the court of appeals’ decision in effect permits some fraud claims to be discharged even if they have been reduced to judgment, a result inconsistent even with the narrow fraud exception of the 1898 statute.

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defrauding debtor would undermine Congress's express policy judgment that the victims of the debtor's fraud should be protected from discharge of the debt owed them by the bankrupt.

B. A Preponderance Standard of Proof for Proceedings Under Section 523 Is Consistent with Section 727 of the Bankruptcy Code and Important Non-bankruptcy Fraud Statutes

1. Although the Bankruptcy Code and its legislative history are silent as to the standard of proof in a Section 523(a) proceeding based on fraud, the legislative history of Section 727 of the Code, 11 U.S.C. 727, suggests that Congress intended a preponderance standard to apply under Section 523(a). Section 727 authorizes the bankruptcy court to grant a discharge in a Chapter 7 liquidation proceeding except in certain circumstances. One exceptional circumstance arises where the debtor has engaged in conduct that would operate as a fraud on the bankruptcy court. 11 U.S.C. 727(a)(4).¹¹ Both the House and the Senate Reports state that "[this] ground for denial of discharge is the commission of a bankruptcy crime, though the standard of proof is preponderance of the evidence rather than proof beyond a reason-

¹¹ Specifically, Section 727(a)(4) denies the debtor a discharge if:

the debtor knowingly and fraudulently, in or in connection with the case—

- (A) made a false oath or account;
- (B) presented or used a false claim;
- (C) gave, offered, received, or attempted to obtain money, property, or advantage, or a promise of money, property, or advantage, for acting or forbearing to act;
- (D) withheld from an officer of the estate entitled to possession under this title, any recorded information, including books, documents, records, and papers, relating to the debtor's property or financial affairs.

Section 152, 18 U.S.C., imposes criminal liability on a debtor who engages in the above conduct.

able doubt." H.R. Rep. No. 595, 95th Cong., 1st Sess. 384 (1977); S. Rep. No. 989, 95th Cong., 2d Sess. 99 (1978). Congress thus instructed the bankruptcy court to deny a discharge as to *all* debts if it determines, *by a preponderance of the evidence*, that the debtor has committed certain fraudulent acts.¹² Section 523(a) merely excepts from discharge particular debts based on fraudulent conduct. Given that Congress instructed the courts to apply a preponderance standard for fraud under Section 727—when the consequence is total ineligibility for discharge—it is unlikely that Congress would have applied a higher standard of proof under Section 523—when the consequence is simply to except from discharge a particular debt.¹³

2. In the absence of clear congressional direction, this Court has declined to construe the Bankruptcy Code so as to create "an extraordinary exemption from non-bankruptcy law." *United States v. Ron Pair Enterprises, Inc.*, 109 S. Ct. 1026, 1032 (1989) (quoting Mid-

¹² Prior to enactment of the Bankruptcy Code, the courts of appeals held that the preponderance standard applied in this context. See, e.g., *In re Robinson*, 506 F.2d 1184, 1187 (2d Cir. 1974); *Union Bank v. Blum*, 460 F.2d 197, 200-201 (9th Cir. 1972). The Code codified this understanding. Remarkably, some bankruptcy courts have refused to give effect to the plain statements in the legislative history or the pre-Code decisions of the courts of appeals. See, e.g., *In re Garcia*, 88 Bankr. 695, 699 (Bankr. E.D. Pa. 1988) (citing cases). These decisions are plainly wrong.

¹³ The preponderance standard in Section 727 also belies the notion underlying the decision below that Congress must have legislated against the backdrop of a "prevailing view" that fraud had to be proved by clear and convincing evidence. Section 727—like Section 523—is silent as to the standard of proof, yet Congress plainly intended the preponderance of the evidence standard to apply. See H.R. Rep. No. 595, *supra*, at 384; S. Rep. No. 989, *supra*, at 99. It seems likely that the only reason Congress expressly stated its intent in the legislative history of Section 727 was that the fraud covered by that section is also subject to criminal sanctions under 18 U.S.C. 152, a concern not presented in the same manner with respect to Section 523.

lantic Nat'l Bank v. New Jersey Dep't of Environmental Protection, 474 U.S. 494, 501 (1986)). Application of the clear and convincing evidence standard in Section 523 proceedings based on fraud would in effect exempt debtors in bankruptcy from important federal non-bankruptcy laws that require proof of fraud only by a preponderance of the evidence. For example, Congress has provided expressly that the preponderance standard shall apply in fraud actions brought by the United States under the False Claims Act. See 31 U.S.C. 3731(c). Similarly, Congress enacted FIRREA in 1989, Pub. L. No. 101-73, 103 Stat. 183, in part “[t]o strengthen the * * * penalties for defrauding or otherwise damaging [financial] institutions and their depositors.” Joint Explanatory Statement of the Committee of Conference, 135 Cong. Rec. H5172, H5174 (daily ed. Aug. 4, 1989); see 12 U.S.C. 1818(i) (expanding civil penalties for bank fraud); 12 U.S.C. 1833a(e) (expressly providing that preponderance standard applies to civil actions brought by the Attorney General to recover civil penalties for certain fraudulent conduct involving financial institutions). The FDIC obtains judgments for civil fraud against persons who defraud banks or thrift institutions under a variety of provisions; including the money penalty provisions of the FDIA, 12 U.S.C. 1818(i), 1821(k)-(l), the securities laws, the civil provisions of the RICO statute, and the antifraud provisions of the Commodity Exchange Act (CEA). Claims under each of these provisions generally are subject to proof by a preponderance of the evidence.¹⁴ In addition, this Court has held that the preponderance standard applies in cases, such as the prior litigation at issue here, brought under Section 10(b) of the Securities Exchange Act and Com-

¹⁴ See *United States v. Local 560, Int'l Bhd. of Teamsters*, 780 F.2d 267, 279 n.12 (3d Cir. 1986) (RICO); *First Nat'l Monetary Corp. v. Weinberger*, 819 F.2d 1334, 1340 (6th Cir. 1987) (CEA). In addition, the FDIC pursues state law remedies for fraud in states that require proof of common law fraud only by a preponderance of the evidence.

mission Rule 10b-5, *Herman & MacLean v. Huddleston*, *supra*.¹⁵

The clear and convincing evidence standard, if adopted by this Court, would require fraud victims who have successfully litigated fraud claims under the preponderance standard prescribed for various important antifraud statutes to litigate their claims anew, under a higher standard of proof, in the bankruptcy court. The Court should decline to adopt a standard of proof in discharge exception proceedings that is “in clear conflict with * * * federal laws of great importance.” *United States v. Ron Pair Enterprises, Inc.*, 109 S. Ct. at 1033.¹⁶

¹⁵ Congress has enacted significant additional securities antifraud legislation without disturbing the *Huddleston* holding. See H.R. Rep. No. 355, 98th Cong., 1st Sess. 15-16 (1983) (report accompanying the Insider Trading Sanctions Act of 1984, Pub. L. No. 98-379, 98 Stat. 1264).

¹⁶ Such wasteful relitigation would be minimized by applying a preponderance standard in Section 523(a) proceedings. If the creditor has obtained a judgment for fraud in a prior proceeding, under either the preponderance standard or the clear and convincing standard, relitigation in the bankruptcy court will be barred by principles of collateral estoppel so long as the identical issues were actually and necessarily determined in the prior litigation. If the plaintiff has litigated and lost a fraud claim in a prior proceeding, under either standard of proof, relitigation would not be permitted in the bankruptcy court. This is so because Section 523 does not provide a substantive cause of action for fraud. The fraud victim's claim must arise out of federal securities law, state common law, or some other nonbankruptcy source of law with its own standard of proof. If the plaintiff has failed to establish a right to recover in the prior litigation, there is no debt to be excepted from discharge. See *Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 161 (1946) (whether “claims of creditors are valid and subsisting obligations against the bankrupt” is generally determined by reference to state law).

II. APPLICATION OF THE CLEAR AND CONVINCING EVIDENCE STANDARD TO THE FRAUD EXCEPTION TO DISCHARGE WAS NOT A WELL-ESTABLISHED PRE-CODE BANKRUPTCY PRACTICE

In construing the Bankruptcy Code, this Court has said that, absent clear direction from Congress, it will look to well-established judicial interpretations under prior bankruptcy law. See *Pennsylvania v. Davenport*, 110 S. Ct. 2126, 2133 (1990); *Kelly v. Robinson*, 479 U.S. 36, 47 (1986); *Midlantic Nat'l Bank v. New Jersey Dep't of Environmental Protection*, 474 U.S. 494 (1986). In this case, the court of appeals presumed that Congress was aware at the time of enacting Section 523 that the "prevailing view" was that fraud had to be proved by clear and convincing evidence in both discharge exception proceedings and common law actions for damages. Pet. App. 13a. The fundamental difficulty with the court's analysis is that there was no established judicial practice of requiring that fraud exceptions to discharge be proved by clear and convincing evidence. In fact, the courts were and are divided over the standard of proof applicable in civil fraud actions generally, and in bankruptcy exception proceedings in particular. What is more, there is no indication that Congress was made aware of judicial decisions articulating the pertinent standard of proof, or focused on this issue at all.¹⁷

¹⁷ In addition, a clear and convincing standard for fraud could lead to application of different standards of proof to the various exceptions to discharge enumerated in Section 523(a). Several of the ten categories of excepted debts set out in Section 523(a) are unrelated to fraud. See, e.g., 11 U.S.C. 523(a)(1)(A)-(B) (certain tax liabilities), 523(a)(5) (alimony and child support), 523(a)(6) (certain educational loans), 523(a)(9) (judgment or consent decree for driving while intoxicated). There is no indication that Congress intended some excepted debts to be treated less favorably than others. Consequently, the Court should hesitate to require that some

A. The Standard of Proof Applicable to Fraud Exceptions to Discharge Was Not Well-Established Prior to 1978

1. Prior to 1970, the bankruptcy courts shared with the state courts concurrent jurisdiction to determine whether a debt was excepted from discharge because it arose from the debtor's fraudulent conduct. As a matter of practice, however, the bankruptcy courts generally did not decide whether particular debts were excepted from discharge. See 1A J. Moore, J. Mulder & L. King, *Collier on Bankruptcy* ¶ 17.28, at 1726-1727 (14th ed. 1978). Instead, the dischargeability question typically was litigated in the state courts, in one of two situations. First, a creditor who had obtained a fraud judgment prior to the bankruptcy proceeding might seek to enforce the judgment in state court after the debtor received a discharge. The debtor would then invoke the discharge as a defense to the enforcement action. See, e.g., *First-Citizens Bank & Trust Co. v. Parker*, 232 N.C. 512, 61 S.E.2d 441 (1950); *Morris v. Levin*, 302 Ill. App. 173, 23 N.E.2d 779 (1939). Second, the creditor might wait until after the debtor emerged from bankruptcy to sue for fraud. Again, the debtor would invoke his discharge as a defense to that action. See, e.g., *Atlas Credit Corp. v. Miller*, 216 So. 2d 100 (La. Ct. App. 1968); *Household Finance Corp. v. Altenberg*, 5 Ohio St. 2d 190, 214 N.E.2d 667 (1966). In both situations, a significant

exceptions be proved by clear and convincing evidence while others require proof only by a preponderance of the evidence.

Indeed, a clear and convincing standard for fraud might lead to application of different standards of proof under Section 523(a)(2). That provision excepts from discharge not only debts incurred through fraud, but debts incurred as a result of "false pretenses, a false representation, or actual fraud." (Emphasis supplied). The most natural interpretation of this disjunctive language is that Section 523(a)(2) excepts certain debts in addition to those incurred as a result of "actual fraud." Thus, cases considering the standard of proof applicable to allegations of actual fraud may not apply to all excepted debts under Section 523(a)(2).

number of courts—often simply applying the standard of proof applicable in the underlying state cause of action to the defense of discharge—required the creditor to prove fraud only by a preponderance of the evidence. See, e.g., *Sweet v. Ritter Finance Co.*, 263 F. Supp. 540, 543 (W.D. Va. 1967); *Nickel Plate Cloverleaf Federal Credit Union v. White*, 120 Ill. App. 2d 91, 92-94, 256 N.E.2d 119, 120-121 (1970); *Gonzales v. Aetna Finance Co.*, 86 Nev. 271, 468 P.2d 15 (1970); *Beneficial Finance Co. v. Machie*, 6 Conn. Cir. Ct. 37, 40-41, 263 A.2d 707, 710 (1969); *Budget Finance Plan v. Haner*, 92 Idaho 56, 59, 436 P.2d 722, 725 (1968); *Mac Finance Plan, Inc. v. Stone*, 106 N.H. 517, 521-522, 214 A.2d 878, 882 (1965); *Atlas Credit Corp. v. Miller*, *supra*; *Household Finance Corp. v. Altenberg*, *supra*.¹⁸ See also *Ames v. Moir*, 138 U.S. 306, 312 (1891) (affirming determination that a debt was excepted from discharge under the 1867 Bankruptcy Act where jury was instructed that it could find fraud by a preponderance of the evidence under state law).¹⁹ Those courts that applied a clear and

¹⁸ Applying the standard of proof applicable to the underlying cause of action for fraud was consistent with the theory that a discharge did not extinguish the debt, but merely provided a defense to the enforcement of the debt. See 1A J. Moore, J. Mulder & L. King, *Collier on Bankruptcy* ¶ 17.27, at 1719 (14th ed. 1978); see also J. Moore & E. Levi, *Gilbert's Collier on Bankruptcy* ¶ 572, at 382-383 (4th ed. 1987) (discussing pleading requirements for asserting discharge as a defense).

¹⁹ In *Oriel v. Russell*, 278 U.S. 358, 362-364 (1929), the Court held that a bankruptcy trustee's right to a "turnover" order must be established by clear and convincing evidence. The Court observed that a charge of failure to turn over property was "equivalent to one of fraud" (*id.* at 362), but the Court's decision rested primarily on the fact that "the [turnover] proceeding is one in which coercive methods by imprisonment [for civil contempt] are probable and are foreshadowed." *Id.* at 363. The Court observed that, in the context of a turnover order, a heightened standard of proof would prevent delays caused by "efforts on the part of bankrupts to retry the issue presented on the motion to turn over." *Ibid.* In the context

convincing standard of proof often did so because the heightened standard applied in that state to proof of fraud in the first instance. See, e.g., *Tek-Ni-Kal Employees Credit Union v. Atkins*, 12 Mich. App. 1, 4, 162 N.W.2d 299, 300 (1968); *Household Finance Corp. v. Williams*, 66 Wash. 2d 183, 185, 401 P.2d 876, 877 (1965); *First Nat'l Bank v. Scieszinski*, 25 Wis. 2d 569, 572, 131 N.W.2d 308, 310 (1964).

2. In 1970, Congress amended the Bankruptcy Act to give the bankruptcy courts exclusive jurisdiction over the dischargeability of certain debts, including debts arising from fraud. Following the 1970 amendments, some federal courts applied the preponderance standard to such claims, see, e.g., *Fierman v. Lazarus*, 361 F. Supp. 477, 480 (E.D. Pa. 1973); *In re Scott*, 1 Bankr. Ct. Dec. (CRR) 581, 583 (Bankr. W.D. Mich. 1975), while others applied the clear and convincing evidence standard of proof, see, e.g., *Brown v. Buchanan*, 419 F. Supp. 199 (E.D. Va. 1975); *In re Arden*, 75 Bankr. 707, 710-711 (Bankr. D.R.I. 1975). Thus, there was no established and consistent practice among courts regarding the standard of proof applied in discharge exception proceedings that Congress could be said to have ratified *sub silentio* in enacting Section 523 in 1978.

Here, no evidence exists that Congress was made aware of any judicial decisions discussing what standard of proof to apply in discharge exception proceedings, let alone decisions applying a clear and convincing standard. And, as set out above, the law as to what standard applied was far from clear. Thus, the court of appeals' "presum[ption]"—based on congressional silence, Pet. App. 13a—was wholly unwarranted.

of Section 523, however, the typical preponderance standard will avoid such delays.

B. The Courts Are Divided Over the Standard of Proof Applicable to Civil Actions for Fraud

Although this Court has referred to the heightened standard of proof "traditionally" imposed in civil fraud cases, see *Cruzan v. Director, Missouri Dep't of Health*, No. 88-1503 (June 25, 1990) slip op. 18 (quoting *Woodby v. INS*, 385 U.S. at 285 n.18), close examination of the cases reveals that, both before and after the enactment of the Bankruptcy Code in 1978, the courts were deeply divided over the appropriate standard of proof in civil actions for fraud. As early as 1943, this Court applied the preponderance of the evidence standard in a civil fraud action under the securities laws. *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 355 (1943) (15 U.S.C. 77q(a)). In addition, both before and after 1978, a significant number of state courts have held that the preponderance standard applies in civil actions for fraud.²⁰ Moreover, several pre-Code treatises state that

²⁰ See *Saxton v. Harris*, 395 P.2d 71, 72 (Alaska 1964); *Sellers v. West-Ark Constr. Co.*, 283 Ark. 341, 343-344, 676 S.W.2d 726, 728 (1984) (preponderance standard in cases tried to a jury; clear and convincing proof needed to cancel or reform a writing in equity); *Clay v. Brand*, 236 Ark. 236, 242-243, 365 S.W.2d 256, 259-260 (1963); *Liodas v. Sahadi*, 19 Cal. 3d 278, 289-290, 562 P.2d 316, 320-324, 137 Cal. Rept. 635, 641-642 (1977); *Kern v. NCD Indus., Inc.*, 316 A.2d 576, 582 (Del. Ch. 1973); *Nye Odorless Incinerator Corp. v. Felton*, 35 Del. 236, 162 A. 504 (1932); *Watson Realty Corp. v. Quinn*, 452 So. 2d 568, 569 (Fla. 1984); *Rigot v. Bucci*, 245 So. 2d 51, 53 (Fla. 1971); *City Dodge, Inc. v. Gardner*, 232 Ga. 766, 770, 208 S.E. 2d 794, 798 (1974); *Milligan v. Milligan*, 209 Ga. 743, 744, 76 S.E.2d 18, 19 (1953) (fraud "being in itself subtle, slight circumstances may be sufficient to carry conviction of its existence"); *Grissom v. Moran*, 154 Ind. App. 419, 427, 290 N.E.2d 119, 123 (1972); *LaCaze v. Louisiana*, 541 So. 2d 322, 328 (La. Ct. App. 1989); *Atlas Credit Corp. v. Miller*, 216 So. 2d 100, 101 (La. Ct. App. 1968); La. Civ. Code Ann. art. 1957 (West 1987); *Martin v. Guarantee Reserve Life Ins. Co.*, 279 Minn. 129, 137-138, 155 N.W.2d 744, 749 (1968); *Cowan v. Westland Realty Co.*, 162 Mont. 379, 382-383, 512 P.2d 714, 716 (1973); *Tobin v. Flynn & Larsen Implement Co.*,

the preponderance standard applies to many or most civil proceedings involving allegations of fraud.²¹ It is

220 Neb. 259, 262-263, 369 N.W.2d 96, 99 (1985) (preponderance standard applies in actions at law for damages); *Murphy Fin. Co. v. Fredericks*, 177 Neb. 1, 4-5, 127 N.W.2d 924, 926 (1964) (same); *Fischetto Paper Mill Supply, Inc. v. Quigly Co.*, 3 N.J. 149, 155, 69 A.2d 318, 321 (1949) (approving "greater weight of the evidence" instruction); *Medivox Productions, Inc. v. Hoffman-LaRoche, Inc.*, 107 N.J. Super. 47, 69, 256 A.2d 803, 814-815 (1969) (preponderance standard applies in legal actions; clear and convincing standard applies in equitable actions); *Maynard v. Durham & Southern Ry.*, 251 N.C. 783, 787-788, 112 S.E.2d 249, 252 (1960), (preponderance of the evidence sufficient to set aside instrument procured by fraud; clear and convincing proof required to reform instrument) rev'd on other grounds, 365 U.S. 160 (1961); *Household Fin. Corp. v. Altenberg*, 5 Ohio St. 2d at 192-194, 34 Ohio Op. 2d at 348-349, 214 N.E.2d at 669-670 (preponderance standard applies to legal actions for fraud; clear and convincing standard applies to equitable actions); *Ostalkiewicz v. Guardian Alarm*, 520 A.2d 563, 569 (R.I. 1987); *Smith v. Rhode Island Co.*, 39 R.I. 146, 153-154, 98 A. 1, 4 (1916); *General Electric Credit Corp. v. M.D. Aircraft Sales, Inc.*, 266 N.W.2d 548, 550 (S.D. 1978); *Aschoff v. Mobil Oil Corp.*, 261 N.W.2d 120, 125 (S.D. 1977); *Piccadilly Square v. Intercontinental Constr. Co.*, 782 S.W.2d 178, 184 (Tenn. App. 1989); *James v. Joseph*, 156 Tenn. 417, 424, 1 S.W. 2d 1017 (1928); *Wirtz v. Orr*, 575 S.W.2d 66, 70-71 (Tex. Civ. App. 1978); *Wyatt v. Chambers*, 182 S.W. 16, 18 (Tex. Civ. App. 1915). Cf. *Travelers Indem. Co. v. Armstrong*, 442 N.E.2d 349, 361 (Ind. 1982) (clear and convincing evidence required to obtain punitive damages for fraud).

Illinois appears to have required proof of fraud only by a preponderance of the evidence until 1983, although thereafter it has required clear and convincing proof. See *L & S Enterprises Co. v. Great American Ins. Co.*, 454 F.2d 457, 460 (7th Cir. 1971) (preponderance); *Barrett v. Shanks*, 382 Ill. 434, 47 N.E.2d 481 (1943) (same); *Hofmann v. Hofmann*, 94 Ill. 2d 205, 222, 446 N.E. 2d 499, 506 (1983) (clear and convincing).

²¹ See, e.g., 37 Am. Jur. 2d *Fraud and Deceit* § 468 (1968); 37 C.J.S. *Fraud* § 94, 113 (1943); Annotation, *Quantum of Proof in Civil Case on Issue Involving Fraudulent, Dishonest, or Criminal Misappropriation of Property*, 62 A.L.R. 1449 (1929); 2 T. Cooley, *Treatise on the Law of Torts* § 349, at 552-554 (4th ed. 1932); M. Bigelow, *The Law of Fraud and the Procedure Pertaining to the Redress Thereof* 474 (1877).

true that a majority of the States require that fraud be proved by more than a preponderance of the evidence, but the majority is far from overwhelming.²² Even in these States, moreover, courts sometimes apply a preponderance standard.²³ In other cases, the court's formula-

²² See *D.H. Holmes Dep't Store v. Feil*, 472 So. 2d 1001 (Ala. 1985); *Rhoads v. Harvey Publications, Inc.*, 145 Ariz. 142, 700 P.2d 840 (1984); *Ficor, Inc. v. McHugh*, 639 P.2d 385 (Colo. 1982); *Miller v. Appleby*, 183 Conn. 51, 55, 438 A.2d 811, 813 (1981) ("clear and satisfactory evidence"); *Pyne v. Jamaica Nutrition Holdings, Ltd.*, 497 A.2d 118 (D.C. 1985); *Dobison v. Bank of Hawaii*, 60 Haw. 225, 587 P.2d 1234 (1978); *Magic Valley Potato Shippers v. Continental Ins.*, 112 Idaho 1073, 739 P.2d 372 (1987); *Beeck v. Aquaslide 'N' Dive Corp.*, 350 N.W.2d 149, 155 (Iowa 1984) ("preponderance of clear, satisfactory, and convincing evidence"); *Stauth v. Brown*, 241 Kan. 1, 734 P.2d 1063 (1987); *Sanford Constr. Co. v. S & H Contractors, Inc.*, 443 S.W.2d 227 (Ky. 1969); *Butler v. Poulin*, 500 A.2d 257 (Me. 1985); *Peurifoy v. Congressional Motors, Inc.*, 254 Md. 501, 255 A.2d 332 (1969); *Transitron Elec. Corp. v. Hughes Aircraft Co.*, 649 F.2d 871 (1st Cir. 1981) (Massachusetts law); *Hi-Way Motor Co. v. International Harvester Co.*, 398 Mich. 330, 247 N.W.2d 813 (1976); *Tietjens v. General Motors Corp.*, 418 S.W.2d 75 (Mo. 1967); *Lubbe v. Barba*, 91 Nev. 596, 540 P.2d 115 (1975); *Caledonia, Inc. v. Trainor*, 123 N.H. 116, 459 A.2d 613 (1983); *Snell v. Cornehl*, 81 N.M. 248, 466 P.2d 94 (1970); *Simkuski v. Saeli*, 44 N.Y.2d 442, 377 N.E. 713, 406 N.Y.S. 2d 259 (1978); *Buehner v. Hoeven*, 228 N.W.2d 893 (N.D. 1975); *Tice v. Tice*, 672 P.2d 1168, 1171 (Okla. 1983); *Bausch v. Myers*, 273 Or. 376, 541 P.2d 817 (1975); *Yoo Hoo Bottling Co. v. Leibowitz*, 432 Pa. 117, 247 A.2d 469 (1965); *Davis v. Upton*, 250 S.C. 288, 157 S.E.2d 567 (1967); *Schwartz v. Tanner*, 576 P.2d 873 (Utah 1978); *Bardill Land & Lumber, Inc. v. Davis*, 135 Vt. 81, 370 A.2d 212 (1977); *Gibson v. Gibson*, 207 Va. 821, 153 S.E.2d 189 (1967); *Beckett v. Department of Social & Health Serv.*, 87 Wash. 2d 184, 550 P.2d 529, 531 (1976); *Campbell v. Campbell*, 146 W. Va. 1002, 124 S.E.2d 345, 353 (1962) ("clear and distinct proof"); *Miles v. Mackle Bros.*, 73 Wis. 2d 84, 242 N.W.2d 247 (1976); *Duffy v. Brown*, 708 P.2d 433 (Wyo. 1985).

²³ See, e.g., *Kopeikin v. Merchants Mortgage & Trust Corp.*, 679 P.2d 599, 601 (Colo. 1984) (en banc) (fraudulent concealment); *Goodfellow v. Kattnig*, 533 P.2d 58, 60 (Colo. Ct. App. 1975); *Modern Displays, Inc. v. Hennecke*, 350 Mich. 67, 85 N.W.2d 80

tion of the standard of proof is so confusing that it is difficult to know what standard it applied.²⁴

In short, both the state courts and the bankruptcy courts were divided over the appropriate standard of proof in fraud exception proceedings, as well as in civil actions for fraud. Accordingly, there is no reason to conclude on the basis of Congress's silence that it was implicitly ratifying a well-established practice of requiring proof of fraud in discharge exception proceedings by clear and convincing evidence. There simply was no such well-established practice.

C. The Reasons for Requiring Clear and Convincing Proof in Certain Fraud Actions are Inapplicable in Section 523 Proceedings

As this Court has recognized, the practice of requiring a heightened standard of proof in certain civil proceedings involving fraud appears to have arisen in actions in which a court of equity was requested to grant relief on claims that were unenforceable at law for failure to comply with the Statute of Frauds, the Statute of Wills, or the parol evidence rule. See *Herman & MacLean v. Huddleston*, 459 U.S. at 388 n.27. A higher standard of proof subsequently was applied in actions seeking to set aside or alter the terms of written instruments. The heightened proof requirement was employed in such

(1957); *Goodrich v. Waller*, 314 Mich. 456, 22 N.W.2d 862 (1946); *In re Delligan's Estate*, 111 Vt. 227, 234-235, 13 A.2d 282, 287 (1940).

²⁴ See, e.g., *Arnett v. Sanderson*, 25 Ariz. 433, 444, 218 P. 986, 990 (1923) ("It is true that proof of fraud should be clear and convincing, but this does not mean that the clear and convincing proof is not to be by a preponderance of the evidence; in fact, fraud is determined by a preponderance of the evidence."); *Gilbert v. Mid-South Machinery Co.*, 267 S.C. 211, 222-223, 227 S.E.2d 189, 194 (1976) ("Fraud must be established by a preponderance of the evidence * * * and, while the evidence must be clear and convincing, such clear and convincing proof may be met by a preponderance of the evidence.") (quoting 87 C.J.S. *Fraud* § 114a (1943)).

cases because they were believed to involve special dangers that claims might be fabricated. *Ibid.* (citing Note, *Appellate Review in the Federal Courts of Findings Requiring More than a Preponderance of the Evidence*, 60 Harv. L. Rev. 111, 112 (1946)). In these cases, the courts were concerned to protect the validity of written instruments and the reliance placed upon such documents.²⁵

The reasons for requiring proof by clear and convincing evidence have little relevance in proceedings to except a debt from discharge under the Bankruptcy Code. In many cases, including this one, the validity of a written instrument is not at issue. In addition, many important federal antifraud provisions "are not coextensive with common-law doctrines of fraud." *Huddleston*, 459 U.S. at 388-389. In fact, as the Court observed in *Huddleston*, statutory remedies for fraud were enacted precisely because of the shortcomings of common law fraud remedies. *Id.* at 389. Accordingly, arguments based on the common law of fraud have little application in the context of a bankruptcy proceeding under Section 523(a).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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²⁵ The Court noted this history in *Cruzan v. Director, Missouri Dep't of Health*, No. 88-1503 (June 25, 1990), slip op. 18, and has applied a heightened standard of proof to protect the integrity of formal documents in earlier cases. See *United States v. American Bell Tel. Co.*, 167 U.S. 224 (1897) (suit to set aside a patent); *Southern Dev. Co. v. Silva*, 125 U.S. 247 (1888) (suit to rescind a land purchase contract).